MARYLAND
DEPARTMENT OF
BUDGET & MANAGEMENT

ROBERT L. EHRLICH, JR.
Governor

MICHAEL S. STEELE
Lieutenant Governor

CECILIA JANUSZKIEWICZ
Secretary

JOHN M.WASILISIN
Deputy Secretary

STATE RESERVE FUND

Testimony of Cecilia Januszkiewicz, Secretary
Senate Budget and Taxation Committee
February 2, 2006

The Spending Affordability Committee and the Department of Legislative Services have recommended that the minimum level of the Rainy Day Fund be increased from 5% of general fund revenues to 7.5% of general fund revenues. This would increase the minimum amount in the Rainy Day Fund to almost $1 billion. We believe that adopting this recommendation will create a problem rather than solve one.

The rationale for this recommendation is that in recent years the Rainy Day Fund has not been used for its statutory purpose of providing resources to resolve the State's difficult fiscal situation because maintaining the minimum balance has become sacrosanct to assuage the rating agencies. The only thing that increasing the minimum balance from 5% to 7.5% would assure is that the State would have more funds in the Rainy Day Fund.

Increasing the minimum balance of the Rainy Day Fund would not make the Governor any more likely to use the Fund unless it exceeds the statutory minimum balance which would now be 7.5% instead of 5%. Further, increasing the minimum balance would not enhance the State's bond rating because the State already has the highest possible bond rating. The bond rating agencies have never suggested that the State should increase the size of the Fund or that the Fund is insufficient. The rating agencies have been satisfied with the way in which the State has managed difficult economic circumstances as evidenced by the reaffirmation over the last 3 years of the State's AAA bond rating by all three rating agencies.

Implementation of this recommendation has one certain result: it will reduce the resources available to balance the FY 2008 budget by $321 million. Rather than solving any problem, increasing the Rainy Day Fund balance to almost $1 billion will thereby create a problem.

The analyst's comment that the proposed fiscal year 2007 general fund balance of $32 million is inadequate to cover potential FY 2007 deficiencies is curious. It has been extremely rare that the enacted budget reflected a General Fund balance sufficient to fund deficiencies at the levels that commonly occur. Since 1980, the general fund balance in budgets enacted by the General Assembly have been sufficient to cover the subsequent deficiencies in only 3 years –

~Effective Resource Management~
45 Calvert Street • Annapolis, MD 21401-1907
Tel: (410) 260-7041 • Fax: (410) 974-2585 • Toll Free: 1 (800) 705-3493 • TTY Users: call via Maryland Relay
http://www.dbm.maryland.gov

1989, 1997, and, of course, 2006. Thus, the size of the general fund balance in the FY 2007 budget is consistent with balances enacted over the last 27 years.

The recommendation to limit withdrawals from the Rainy Day Fund to $200 million is also unwise and counterproductive. There is some question as to whether such a restriction is effective to limit transfers in future fiscal years. The Governor's budget includes a $670 million allowance in the Dedicated Purpose Account specifically because these funds will be needed in FY 2008. In developing the FY 2007 budget, the Governor intended to insure that the fiscal situation in FY 2008 would be manageable. If effective in FY 2008, this restriction will increase the likelihood of significant budget reductions in FY 2008 because it would limit the use of resources for FY 2008 operations. Therefore, we recommend that this recommendation be rejected.

We also believe that it would show foresight and prudent planning for the Committee to reject the recommendation to delete the $670 million allowance to the Dedicated Purpose Account Reserved for FY 2008 operations. Appropriating these funds as allowed in the budget would make it clear that these funds are to be used for that purpose.

The funds identified for increasing the Rainy Day Fund balance have already been allocated to obligations the State will face in FY 2008. Moreover, there is no benefit to increasing the Rainy Day Fund balance because the State's bond rating is already the highest rating. For these reasons, we urge the Committee to retain the minimum Rainy Day Fund balance at 5% of general fund revenues. For FY 2007, this amount is $644 million. We also urge that the Committee reject the recommendation to eliminate the allowance for the reserve for fiscal year 2008 operations.